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**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	Rulemaking 06-04-009 (Filed April 13, 2006)

California Energy Commission Docket #07-OIIP-01

REPLY COMMENTS OF THE NATURAL RESOURCES DEFENSE COUNCIL (NRDC), UNION OF CONCERNED SCIENTISTS (UCS) AND GREEN POWER INSTITUTE (GPI) ON TYPE AND POINT OF REGULATION ISSUES FOR THE NATURAL GAS SECTOR

January 8, 2007

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I. Introduction and Summary

The Natural Resources Defense Council (NRDC), Union of Concerned Scientists (UCS) and Green Power Institute (GPI) respectfully submit these reply comments in accordance with the "Administrative Law Judges' Ruling Requesting Comments on Type and Point of Regulation Issues for the Natural Gas Sector" (ALJ Ruling), dated November 28, 2007; and pursuant to Rules 1.9 and 1.10 of the California Public Utilities Commission's (CPUC) Rules of Practice and Procedure. NRDC/UCS/GPI also concurrently submit these comments to the California Energy Commission (CEC) in Docket #07-OIIP-01, the CEC's sister proceeding to this CPUC proceeding.

NRDC is a non-profit membership organization with a long-standing interest in minimizing the societal costs of the reliable energy services that a healthy California economy needs. In this proceeding, NRDC represents its more than 124,000 California members' interest in receiving affordable energy services and reducing the environmental impact of California's energy consumption. UCS is a leading science-based non-profit working for a healthy environment and a safer world. Its Clean Energy Program examines the benefits and costs of the country's energy use and promotes energy solutions that are sustainable both environmentally and economically. The Green Power Institute (GPI) is the renewable energy program of the Pacific Institute, a leading environmental research and advocacy institution that is active in water and energy issues. The GPI has performed pioneering research on the greenhouse gas implications of renewable energy production.

In summary, our comments elaborate on the following key points:

- ♦ Including the natural gas sector in a cap and trade system will guarantee that the sector will not exceed a certain level of emissions by 2020.
- ♦ California should move forward with a cap and trade system that includes the natural gas sector.
- ♦ The natural gas sector should be included in a cap and trade system, not left outside the system to provide offsets.
- ♦ End-users with emissions over 10,000 metric tons of CO2e should be regulated as point sources.
- ♦ The Commissions should address life-cycle emissions from liquefied natural gas (LNG).

II. Including the natural gas sector in a cap and trade system will guarantee that the sector will not exceed a certain level of emissions by 2020.

NRDC/UCS/GPI agree with the many other commenters who enumerated the value of a cap and trade program and support inclusion of the natural gas sector in such a program. *See* Edison Comments at 4; SMUD Comments at 1; Indicated Producers Comments at 3; CalSEIA and SRCC Comments at 2-3; Green Power Institute Comments at 2; Community Environment (CE) Council Comments at 3-4. Contrary to PG&E and Southwest Gas' contentions (*see* PG&E Comments at 3 and Southwest Gas Comments at 3), there are numerous emissions reduction strategies in the natural gas sector. *See* NRDC/UCS Comments at 8-9, 17. Including the natural gas sector in a cap and trade program will guarantee that the sector does not exceed a certain level of emissions by 2020, which intensity-based programmatic measures will help to achieve but will not guarantee.

III. California should move forward with a cap and trade system that includes the natural gas sector.

NRDC/UCS/GPI believe that California should move forward with a cap and trade system that includes natural gas, even if regional and federal programs have not yet emerged. To the extent that El Paso is suggesting that California should not take action until regional and national programs are developed, NRDC/UCS/GPI disagree. *See* El Paso Comments at 3 ("Waiting to see how [regional or federal] programs develop could improve consistency between the programs and reduce the need to revise or revamp California's program.") California has put herself squarely at the forefront of efforts to develop policies to combat climate change, and absolutely should continue to participate and lead at the regional and national levels. That way California will not have to wait for broader-scale programs to germinate and develop, and then adjust accordingly. Instead, California will ensure that the broader-scale programs are developed in ways that build on and incorporate the early actions we have taken.

IV. The natural gas sector should be included in a cap and trade system, not left outside the system to provide offsets.

NRDC/UCS/GPI disagree with San Diego Gas and Electric's (SDG&E) suggestion that small end-users of natural gas should be able to participate in a cap and trade system by providing offsets, but should not be included in the cap and trade system. *See* SDG&E Comments at 5. SDG&E implies that the individual end-users themselves would be selling offsets into the cap and trade market. It would be more efficient and effective for LDCs to participate in the market (and be required to hold allowances) on behalf of their end-use customers.

Offsets, by definition, can only be considered for sectors that are not included in a cap and trade program. Offsets present many administrative difficulties and we believe there are other better policy tools (such as performance standards) that should be used to achieve reductions in sectors of the economy that can not be included in the cap and trade system. Offsets are, at best, a "zero sum game" that allow higher emissions within the capped sectors and substitute reductions in uncapped sectors, and do not provide any *additional* emission reductions towards the AB 32 statewide emissions limit. Leaving end-users of natural gas outside the cap and trade system with the option to sell offsets back in to the system would mean that the cap for those sectors in the cap and trade system would have to be set more tightly in order to ensure that the state reaches the emissions limit under AB 32.

Offsets are essentially a funding mechanism to draw funds from capped sectors into uncapped sectors to provide incentives for emission reductions. The natural gas sector can and should contribute to meeting the statewide emissions limit rather than asking other sectors to fund its contribution. LDCs can participate in a cap and trade system, and it will make the entire system more effective and more administratively manageable to include them in the system rather than allowing them to participate through offsets.[1] We urge the Commissions to use both programmatic measures, such as efficiency programs and solar water heating, to help individual customers reduce emissions, and a cap and trade program to limit emissions from the natural gas sector.

V. End-users with emissions over 10,000 metric tons of CO2e should be regulated as point sources.

NRDC/UCS/GPI agree with the many other commenters who advocated large end-users of natural gas be regulated as point sources. *See* Edison Comments at 6; PG&E Comments at 2; SDG&E Comments at 8; El Paso Comments at 3; CE Council Comments at 10. Currently, CARB's threshold for stationary source reporting is 25,000 metric tons CO_2e. NRDC/UCS/GPI believe that, ultimately, 10,000 metric tons CO_2e is a better threshold for stationary sources, because it is consistent with existing utility thresholds and with proposed federal legislation, and because it captures more large end-users with the capacity to report and make reductions. *See* NRDC/UCS Comments at 12. Wild Goose Storage points out that CARB estimates that lowering the threshold to 10,000 would double the number of reporting entities (Wild Goose Comments at 6), but this would only result in a total of approximately 300 reporting entities, fewer than 120 of

[1] Market Advisory Committee, *Recommendations for Designing a Greenhouse Gas Cap-and-Trade System for California*, June 30, 2007, p. 74 ("the number of staff needed to implement an effective offset monitoring program could conceivably by larger than the staff needed to run the cap-and-trade program itself.")

whom would be natural gas end-users.[2] This would be administratively feasible. LDCs should be responsible for the emissions associated with all end-users of natural gas below CARB's stationary source threshold.

VI. The Commissions should address life-cycle emissions from liquefied natural gas (LNG).

Community Environmental Council advocates life-cycle analysis for LNG. *See* CE Council Comments at 12-13. As CE Council notes, CARB is planning to assess fuels in the transportation sector on a life-cycle basis as part of the Low Carbon Fuel Standard. *See* CE Council Comments at 13. NRDC/UCS/GPI support the use of life-cycle analysis where it is both useful to effectively implement the goals of a policy, and feasible. A recent study of life-cycle emissions of electricity generation shows that average life-cycle emissions from LNG are approximately 10% to 30% higher than average life-cycle emissions for domestic sources of natural gas, depending on the source of the LNG.[3] Therefore, we agree with CE Council that measuring lifecycle emissions for LNG may be useful in implementing a cap and trade program and minimizing emissions leakage.

At the same time, we recognize that the Commissions already have an ambitious schedule in this proceeding to develop the priority program design issues to contribute to CARB's scoping plan, and we urge the Commissions not to delay this schedule. As soon as possible (for example, as the next phase of this proceeding), we urge the Commissions to develop the technical basis necessary to address lifecycle emissions, and then to work with CARB, the California Climate Action Registry, and stakeholders to integrate it into CARB's reporting requirements and the overall program.

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[2] California Air Resources Board Staff, *Proposed Regulation for Mandatory Reporting of Greenhouse Gas Emissions Pursuant to the California Global Warming Act of 2006 (Assembly Bill 32),* October 19, 2007, p. 53; CARB Workgroup on Reporting, General Stationary Combustion GHG Emissions presentation June 25, 2007, slide 20; *See* NRDC/UCS Comments at 12.

[3] Paulina Jaramillo, et al, *Comparative Life-Cycle Air Emissions of Coal, Domestic Natural Gas, LNG, and SNG for Electricity Generation*, 41 (17) ENVIRON. SCI. TECHNOL. 6290, 6293 (2007) (calculating the average life-cycle emission factor is 1250 lb CO2e/MWh for domestic natural gas and 1600 lb Co2e/MWh for LNG.

VII. Conclusion

NRDC, UCS and GPI appreciate the Commissions' efforts to design GHG emissions regulation for the natural gas sector that meet the expressed criteria. We urge the Commissions to use both programmatic measures and a cap and trade program to limit emissions from the natural gas sector.

Dated: January 8, 2007

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the **"Reply Comments of the Natural Resources Defense Council (NRDC), Union of Concerned Scientists (UCS) and Green Power Institute (GPI) on Type and Point of Regulation Issues for the Natural Gas Sector" in the matter of R.06-04-009** to all known parties of record in this proceeding by delivering a copy via email or by mailing a copy properly addressed with first class postage prepaid.

Executed on January 8, 2007 at San Francisco, California.

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